No. 15-628

In The

Supreme Court of the United States

BASSAM YACOUB SALMAN,

Petitioner,

v.

UNITED STATES OF AMERICA,

Respondent.

On Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

BRIEF FOR PETITIONER

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QUESTION PRESENTED

Does the personal benefit to the insider that is necessary to establish insider trading under *Dirks v. SEC*, 463 U.S. 646 (1983), require proof of "an exchange that is objective, consequential, and represents at least a potential gain of a pecuniary or similarly valuable nature," as the Second Circuit held in *United States v. Newman*, 773 F.3d 438 (2d Cir. 2014), *cert. denied*, No. 15-137 (U.S. Oct. 5, 2015), or is it enough that the insider and the tippee shared a close family relationship, as the Ninth Circuit held in this case?

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INTRODUCTION

This case calls upon the Court—as it has done repeatedly in recent years—to impose clear limits on a federal crime that rests on indeterminate statutory language. The Court has used several interpretive tools to cabin elastic federal crimes, including careful reading of the statutory text, strict enforcement of the prohibition on common-law crimes, and application of the rule of lenity and the doctrine of constitutional avoidance. These interpretive tools rest on two main constitutional foundations: the separation-of-powers principle that it is for Congress, and not the courts, to enact federal criminal laws, and the due process prohibition on vague criminal statutes. The judge-made crime of "insider trading" implicates both of these constitutional principles.

Section 10(b) of the Securities Exchange Act of 1934 prohibits the use of a "manipulative or deceptive device or contrivance" in connection with the purchase or sale of a security, but is silent on "insider trading." This Court has repeatedly held that merely trading securities based on material nonpublic information is neither "deceptive" nor "manipulative," and that §10(b) therefore imposes no general duty to refrain from trading on inside information. The Court has, however, found in §10(b) certain limited situations in which a corporate insider's trading, as well as "tipping" and trading by a "tippee" of a corporate insider, can violate the statute. In *Dirks v. SEC*, 463 U.S. 646 (1983), the Court held that tippees may freely trade on material nonpublic information unless that information came

from an insider who breached his fiduciary duty to the company's shareholders by disclosing it for "personal gain," and the tippee knows these facts. This personal benefit requirement is the line demarcating when tippee trading on material nonpublic information is legal, and when it is fraud that violates §10(b). Importantly, the focus in ascertaining whether the government has proved the requisite benefit is on the tipper's motive.

Petitioner Bassam Salman was convicted of securities fraud offenses on the theory that he engaged in criminal insider trading. Salman was not a corporate insider, nor was he "tipped" by an insider. He was a "remote tippee"; he traded on inside information that he learned third-hand from a member of his extended family, Mounir "Michael" Kara, who in turn received it from his brother Maher, a Citigroup banker. Under this Court's precedents, Salman was free to trade on the information unless the original tipper, Maher, shared the information with his brother Michael in exchange for a "personal benefit."

It was undisputed that Michael neither paid Maher nor provided him with anything of value for the information. There was no tangible exchange and, if anything, the conversations were detrimental, not beneficial, to Maher, because they made him anxious and upset. Maher did not want Michael to trade on the information or to share it with anyone else, in one case even provoking Michael to swear "on his daughter's life that he wasn't trading." The government charged only one instance in which Maher even suspected that Michael was trading.

The question in this case is what counts as a personal benefit. Must the benefit represent a concrete, tangible pecuniary gain to the tipper, or is the intangible, emotional "benefit" that one might receive by providing a "gift" of inside information to get a bullying "friend" or "relative" "off one's back" enough, as the Ninth Circuit held?

The answer is that the Court's insider trading cases, like its other fraud precedents, require a showing of pecuniary gain. This narrow definition of personal benefit is necessary to avoid the serious due process and separation-of-powers problems that a broader rule would create. In the three decades since *Dirks*, the government has taken an increasingly expansive view of what might qualify as a "personal benefit." It has filed charges in many cases where the insider received no tangible benefit whatsoever; instead, the alleged "benefit" was social or interpersonal in nature, in that the tippee was the insider's casual acquaintance or relative. Yet most, if not all, insiders have this kind of relationship with their alleged tippees. If such minimal ties to the tippee satisfied the personal benefit requirement, this Court's restrictions on insider trading liability would be meaningless. An insider who tips will *always* have some emotional reaction to his disclosure. Which emotions are beneficial to the insider, and which are not? How is a remote tippee supposed to know the difference?

The Ninth Circuit's indeterminate psychological benefit "standard" provides so much flexibility that it would effectively allow the government to usurp Congress' role to define the

crime. If endorsed, the Ninth Circuit's approach would eliminate the personal benefit requirement, and replace it with precisely the broad prohibition on insider trading that this Court has repeatedly rejected. The Court should instead adopt the only clear and definite personal benefit standard that will enable market participants to discern when they can legally trade, and when they cannot: pecuniary gain to the insider.

OPINIONS BELOW

The relevant opinion of the Ninth Circuit is reported at 792 F.3d 1087. The Ninth Circuit issued an additional opinion that is unpublished, *see* 618 Fed. App'x 886, and the opinion of the U.S. District Court for the Northern District of California is at 2013 WL 6655176.

JURISDICTION

The district court had jurisdiction under 18 U.S.C. §3231. The court of appeals had jurisdiction under 28 U.S.C. §1291. The Ninth Circuit entered judgment on July 6, 2015. A petition for rehearing was denied on August 13, 2015. The petition for writ of certiorari was filed on November 10, 2015 and granted on January 19, 2016. This Court has jurisdiction under 28 U.S.C. §1254(1).

CONSTITUTIONAL, STATUTORY AND REGULATORY PROVISIONS

Relevant constitutional, statutory and regulatory provisions are reprinted in the Statutory Appendix to this brief.

STATEMENT OF THE CASE

This case directly illustrates how the government's expansive reading of §10(b) has gutted the personal benefit requirement. Michael neither paid Maher nor provided him with anything of value for the information. If anything, Michael bullied Maher into leaking the information; the exchanges caused Maher serious anxiety, and he only capitulated to get Michael "off his back." Indeed, the district court reduced Maher's Sentencing Guidelines offense level because Maher "did not benefit, did not engage in this conduct for self-benefit, [and] did not gain anything."[1] Similarly, the SEC concluded that the fact that Maher "received no financial benefit" was a "mitigating circumstance[]" weighing in favor of a temporary, rather than permanent, bar from the securities industry.[2] If a benefit can be divined from these facts, there is no case in which one will not be present, and few cases

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[1] Tr. of Proceedings at 9, *United States v. Kara*, No. 09-cr-00417-EMC-1 (N.D. Cal. Dec. 19, 2014); *id.* at 20 (gain in presentence report "overstate[d]" Maher's "culpability...since he did not engage in trades for personal gain and gained nothing from this in terms of any monetary enrichment").

[2] *Kara*, Initial Decision Release No. 979, 2016 WL 1019197, at *6-7 (ALJ Mar. 15, 2016), *noticed as final decision*, Exchange Act Release No. 77731, 2016 WL 1660190 (Apr. 27, 2016).

in which even remote tippees who had no involvement in or knowledge of the facts underlying the disclosure could avoid criminal liability. Salman had nothing to do with Michael's efforts to obtain the information, knew nothing about the circumstances of Maher's disclosures, and did not know what benefit, if any, Maher might have received.

Nevertheless, the government maintained that Salman violated §10(b) because Maher benefited by disclosing the information as a "gift" to his brother Michael. JA.404-05. Under this theory, Salman was convicted of "insider trading" and conspiracy to commit insider trading, and sentenced to three years' imprisonment.

A. Trial

In September 2011, in the U.S. District Court for the Northern District of California, Salman was charged with four substantive counts of insider trading and one count of conspiracy to engage in insider trading. JA.20-33. Salman was tried in September 2013. Michael and Maher testified for the prosecution under cooperation agreements.

Viewed in the light most favorable to the government, the evidence established that Maher often shared information with Michael in confidence to get advice about work or blow off steam. But the two brothers had a complicated relationship that often taxed Maher. Michael betrayed Maher's trust and persistently pressured him for more information. Maher never disclosed information to Michael for anything of value or as part of a *quid pro*

quo; all Maher ever sought to obtain was the scant comfort of getting Michael to stop pestering him. Maher also had no idea that his brother was relaying information to Salman or anyone else.

Michael testified that he told Salman that at least some of his information came from Maher. But there was no evidence that Michael told Salman how he got the information from Maher, and nothing to suggest to Salman that Michael had bribed Maher or provided him with anything of value for the information.

1. *Michael and Maher.* Michael and Maher were born in Lebanon and emigrated to the United States with their parents in 1976. JA.59. The family settled in the San Francisco Bay Area. *Id.* Michael was eleven years older than Maher, and very protective of his younger brother. JA.195, 215-16. Michael was highly intelligent. He graduated from college at age 20 with a degree in biochemistry and studied toxicology in a graduate program for three years. JA.170, 211-12. But Michael struggled with mental illness for decades and had bouts of substance abuse. *E.g.*, JA.68, 139-43, 148-49, 213-14, 324-28.

Maher excelled in school and business. JA.132, 321-22. He graduated from the University of California at Berkeley in 1993, passed the CPA exam, and went to work for Coopers & Lybrand in New York. JA.63-64. Maher testified that one reason he left the Bay Area was to escape his brother and "the stress that [he] had put on [their] family." JA.65. Maher later attended business school in

Chicago, earned his MBA, and began working at Citigroup as an investment banker in 1998. JA.65-66. Four years later, Maher joined Citigroup's healthcare group as a vice president. JA.67 In that role, Maher advised biotechnology and pharmaceutical companies on mergers, acquisitions and financing strategies. JA.69-70. Maher was in the healthcare group from 2002 to 2007 and became a director during that period. JA.68, 92. He was based mostly in New York. JA.67

Michael remained in California, where he operated a hazardous waste business. JA.212-13, 294. In 2004, Michael took over his father's Charles Schwab account and started actively trading securities, including stock options. JA.221-22, 336-38. He performed his own research and by 2006 was researching 50-60 companies at a time. JA.329; *see* JA.288-89, 330-31.

2. *Maher shared information with Michael for varied reasons.* Maher occasionally shared information about his work with his older brother for a number of reasons.

When Maher first joined the healthcare group, he had no experience in that sector. JA.79. By contrast, Michael was highly knowledgeable in the field given his science background. Maher therefore occasionally sought Michael's advice. JA.79, 150-51. During these conversations, Maher and Michael openly discussed the companies that Citigroup was advising. JA.79-80. Maher gave Michael "clear instructions that [the] information...was confidential, and that [Maher] was really just trying

to gain an industry knowledge through his help." *Id.* Maher believed that conferring with Michael about his work was helpful to Citigroup: Michael's advice helped him become a "much more intelligent officer" who could have "fruitful scientific discussions with the officers of these public corporations." JA.82, 150-51.

As Maher's career progressed, he continued to use Michael as a "soundboard," to "vent about [his] career," and to let his big brother know about his achievements. JA.112, 154. Maher felt "extremely comfortable" discussing his work candidly with Michael. JA.97. Maher repeatedly told Michael that the information he was sharing was confidential. JA.85.

For example, in early 2005 Citigroup was pitching to provide financing for a significant client in an impending acquisition. JA.93-97. The CEO of that client was a wine connoisseur, so Maher asked Michael, who was also a wine enthusiast, to recommend some wines that Maher could present to the CEO as a gift. JA.95-97 It was important to Citigroup and to Maher that Citigroup win this deal, and Maher believed that this gesture—with Michael's help—would improve their chance of success. *Id.* Unbeknownst to Maher, Michael traded on the basis of this information. JA.269-70.[3]

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[3] Maher also came to believe that Michael eavesdropped on his work calls and, at one point, went behind Maher's back and snuck into his briefcase to look at documents related to potential merger and acquisition transactions. JA.160-62.

Maher admitted that in hindsight he may have been "naïve, relaxed, unguarded" with the information he shared, but he trusted Michael not to jeopardize his career by misusing the information. JA.85, 112. In Maher's words: "I just never could imagine that my brother would take it upon himself to trade in the companies that I was covering...we share the same last name, he knew how important the job was to me, how much I cared about it." JA.85.

Additionally, in late 2003, their father was diagnosed with terminal brain cancer. JA.80. The brothers were devastated by the news. They had constant discussions from the time of the diagnosis until their father's passing in November 2004 about drugs and drug companies that might help him. JA.80, 151-53. Michael spent two to three hours every day independently researching drugs and drug companies, and would regularly update Maher with his findings. Tr.1279-80. Maher, for his part, shared information that he had learned through his work. JA.80, 151-53.

Sometime in 2005 Michael began to ask Maher "more targeted" questions about companies and their businesses. JA.80-81. Maher continued to share information with Michael, but only after insisting that Michael promise that he was not trading based on that information. JA.81. Maher testified: "And I confronted him, and asked him point-blank, 'Are you trading in these companies?' And he flat-out denied it, and he swore on his daughter's life that he wasn't trading in it." *Id.*

In 2005 or 2006, Michael increasingly pestered Maher with questions about healthcare companies. *Id.* Maher avoided Michael's phone calls, told his wife not to answer the phone at home, and did not respond to Michael's emails. *Id.* Eventually, Michael's questioning "got to the point where it was so persistent and so nagging," according to Maher, "that to get him off my back....I knowingly tipped him, to get him off my back, and to benefit him." *Id.*; *see* JA.117-18. Even then, however, Michael never told Maher that he was trading on the information, although Maher suspected he was trading. JA.82, 159.

3. *Bassam Salman.* Salman worked as a grocery wholesaler in Chicago throughout the relevant period. JA.137, 284. He met Maher and Michael in 2002 when Salman's sister Sawsan began a relationship with Maher. JA.385-87. Maher and Sawsan married in July 2005. JA.388.

Michael and Salman started discussing stocks in September 2004. JA.254. In those first conversations, Michael told Salman "the names of certain companies that [he] was dealing with on a daily basis. Maybe four or five companies." JA.255. Michael also taught Salman how to trade options. JA.255-56.

Thereafter, Michael gave Salman investment recommendations based on his own research as well as on information that he had obtained from Maher. *See, e.g.*, JA.261-62, 271 73, 275-76, 289-92, 298-99. The government introduced evidence that, using another relative's brokerage account, Salman

engaged in trading that largely paralleled Michael's. JA.262-63, 276, 364. Michael testified that he told Salman that Maher was the source of his "investment strategies" and at least some of his information. JA.257, 266. And even though Michael claimed to have told Salman that Maher was his source, there was no evidence that Michael ever told Salman whether Maher was providing the information to him willingly, or what, if anything, Maher was receiving in return.

4. *The charges.* The substantive charges concerned Salman's trades in securities of United Surgical Partners International, Inc. ("USPI") in November and December 2006 and his trades in securities of Biosite Incorporated ("Biosite") in March 2007. The conspiracy count concerned those two companies as well as Bone Care International, Inc. ("Bone Care") and Andrx Corporation ("Andrx").

a. *Bone Care.* In April 2005, Citigroup was representing Bone Care in its sale to Genzyme Corporation. JA.50-51. Maher testified that he did not recall having any conversations with Michael about Bone Care. JA.99. Michael, however, testified that Maher told him Bone Care would be acquired. JA.278. Michael traded in the stock and also advised Salman to invest. JA.280. Salman followed his recommendation and bought Bone Care stock. JA.365.

b. *Andrx.* In January 2006, Citigroup was representing a company that sought to acquire Andrx. JA.107-08. Maher had worked on the deal extensively but supervisors removed him from the

assignment before the deal closed. He confided to Michael that this made him extremely upset. JA.111 12. Unbeknownst to Maher, Michael invested in Andrx in late February 2006. JA.295. Michael also recommended to Salman that he invest. JA.297. Salman bought call options in Andrx. JA.367.

c. *USPI.* In the summer of 2006, Citigroup was representing USPI's largest shareholder, a private equity firm, which was interested in buying out the other shareholders. JA.113-14. Maher testified that one day in August Michael told him that, based on his own research, USPI "looked cheap." JA.115. Maher agreed and told Michael that USPI was likely to be acquired by a private equity firm. JA.116. Michael bought USPI for himself and recommended it to Salman and others. JA.301, 304-06. Salman bought USPI call options in August 2006. Tr.1590-91. For months after their August conversation, Michael "persistently and repeatedly" called Maher to get more information about USPI. JA.117. Maher testified that he "did everything [he] could to sort of deflect it," but finally Maher caved and indicated that the deal was still progressing. *Id.*; JA.307-08. Michael bought more USPI call options through the fall of 2006 and continued to recommend it to Salman, who purchased additional USPI securities in November-December 2006. JA.306-09, 368-70.

d. *Biosite.* In early 2007, Citigroup was representing a client that was considering purchasing Biosite. JA.122. On March 22, 2007, Maher was in a taxi and returned a telephone call

from Michael from his cell phone. JA.123. Michael "didn't sound well"; he had been very ill and "sounded very down." JA.123-24. Michael said that he needed a favor, and asked Maher for information about a potential transaction. JA.124. This request presented a "sudden and unexpected situation" for Maher, and he was worried for his brother. *Id.* He "panick[ed]" and told Michael that Biosite might be acquired the following week. *Id.* Maher instantly regretted what he had done; he got out of the cab, began pacing on the sidewalk, and called Michael right back. JA.125, 164-65. Maher begged Michael not to act on the information or share it with anyone, to which Michael responded, "Don't worry." JA.125, 332-33.

Michael defied his brother. He traded in Biosite that day and also relayed the information to Salman, who traded, and others. JA.309-10, 313, 333.

5. *Maher was unaware that Michael was tipping others.* Maher did not know that Michael shared any of the information with anyone else. JA.129-31, 159, 168. When he finally learned what Michael had done, Maher felt: "Upset. Shocked. Angry. Defeated. Manipulated. Betrayed." JA.168-69; *see also* JA.143 (describing Michael as a "thief" and a "liar").

6. *Jury instructions and verdict.* The district court instructed the jury that to convict Salman of insider trading it needed to find, among other elements, that (1) the insider (here, Maher) personally benefitted from the disclosure of material,

nonpublic information, and (2) Salman knew that the insider had personally benefitted from the disclosure. Pet.App.59.

The district court instructed that "personal benefit" to the insider could include "the benefit one would obtain from simply making a gift of confidential information to a trading relative or friend." Pet.App.61. The district court further instructed that the jury did not have to find that Salman knew "the specific benefit given or anticipated by the insider in return for disclosure of inside information; rather, it is sufficient that [Salman] had a general understanding that the insider was improperly disclosing inside information for personal benefit." Pet.App.47.

The jury convicted on all counts, and Salman appealed.

B. Appeal

Shortly after Salman filed his reply brief, the Second Circuit decided *United States v. Newman*, 773 F.3d 438 (2d Cir. 2014), *cert. denied*, No. 15-137 (U.S. Oct. 5, 2015). Like this case, *Newman* involved defendants who were remote tippees. The Second Circuit held that the defendants had not committed a crime because the government failed to prove that the alleged tippers received any personal benefit, or that the defendants knew of any such benefit.

The court observed that prior Second Circuit cases indicated that "personal benefit" could include "the benefit one would obtain from simply making a

gift of confidential information to a trading relative or friend"—the same standard applied in Salman's case. *Id.* at 452. But the court found that this standard would contravene *Dirks*. *Id.*

The *Newman* court explained that the government may not "prove the receipt of a personal benefit by the mere fact of a friendship, particularly of a casual or social nature," because "[i]f that were true,...the personal benefit requirement would be a nullity." *Id.* Accordingly, the court held: "To the extent *Dirks* suggests that a personal benefit may be inferred from a personal relationship between the tipper and tippee, where the tippee's trades 'resemble trading by the insider himself followed by a gift of the profits to the recipient,'...we hold that such an inference is impermissible in the absence of proof of a meaningfully close personal relationship that generates an exchange that is objective, consequential, and represents at least a potential gain of a pecuniary or similarly valuable nature." *Id.* And while "the tipper's gain need not be *immediately* pecuniary,...in order to form the basis for a fraudulent breach, the personal benefit received in exchange for confidential information must be of some consequence." *Id.* (emphasis in original).

Applying this standard, the Second Circuit held the evidence of personal benefit insufficient because the insiders in *Newman* had not participated in the requisite *quid pro quo* exchange. *Id.* at 452-53. (The government alleged that one insider had exchanged information with a college friend in exchange for "career advice," and that the other had tipped a friend from church. *Id.*) The

Second Circuit also found that the government failed to prove that the defendants knew of any personal benefit the insiders supposedly received. *Id.* at 453-55. The court thus reversed the convictions. *Id.* at 455.

The Ninth Circuit permitted the parties to file supplemental briefs addressing *Newman*'s effect on Salman's conviction. Salman argued that the evidence of personal benefit to Maher (and Salman's knowledge of any such benefit) was insufficient under *Newman*. Specifically, Salman argued that there was no evidence that Maher engaged in an exchange with Michael that yielded Maher even a potential pecuniary gain.

The Ninth Circuit disagreed. It declined to follow *Newman* and held that the government was not required to prove that the sibling relationship between Maher and Michael "generate[d] an exchange that is objective, consequential, and represents at least a potential gain of a pecuniary or similarly valuable nature." Pet.App.15 ("To the extent *Newman* can be read to go so far, we decline to follow it."). Instead, the court found it sufficient under *Dirks* if the government proved that Maher "'ma[de] a gift of confidential information to a trading relative or friend.'" Pet.App.16 (quoting *Dirks*, 463 U.S. at 664). Holding that the government met this burden, the court affirmed Salman's conviction. Pet.App.16-17.

SUMMARY OF ARGUMENT

The crime of insider trading that Salman was charged with committing is entirely judge-made. Congress was aware of insider trading when it enacted §10(b), but chose *not* to address it in that statute. As a result, §10(b) does not mention insider trading, much less define its elements. The statute prohibits only "manipulative" and "deceptive" conduct in connection with the purchase or sale of securities, and there is nothing inherently manipulative or deceptive about insider trading.

I. Recognizing that "only Congress, and not the courts...can make conduct criminal," *Bousley v. United States*, 523 U.S. 614, 620-21 (1998), this Court has repeatedly held that §10(b) does *not* create any general duty to refrain from trading on material nonpublic information, or entitle all investors in the securities markets to parity of information. The Court has, however, read into §10(b) a very limited proscription on insider trading. Under that narrow rule, a "tippee" must refrain from trading on inside information if, and only if, the information was disclosed by an insider in exchange for personal benefit, *and* the tippee knows that fact. The line between lawful trading and criminal activity, then, is determined by whether the insider—here, Maher—disclosed the information to obtain some personal benefit. If he did not, there was no §10(b) violation, and the "tippee" was free to trade.

II. The Court's reasoning in *Dirks* and other insider trading cases shows that its purpose was to limit §10(b) insider trading and tipping

liability to situations where the tipper sought to make money. Cabining securities fraud liability to circumstances where the tipper seeks remuneration also accords with precedents involving similar crimes, where the Court has required the government to prove that the defendant sought money or property. The focus of these fraud crimes, as here, is the improper exploitation of a fiduciary relationship for personal profit. The facts here involve no such misconduct. Maher did not trade or seek any kickback, and was pressured by his brother to leak the information.

III. Because of the judicial origin of the §10(b) insider trading crime and the indeterminacy of the Ninth Circuit's standard, the question presented implicates profound constitutional separation-of-powers and due process problems. To avoid those problems, the Court should apply well-established principles requiring a narrow construction of criminal statutes, and §10(b) in particular, to limit the ambit of the personal benefit element to core cases where an insider provides a tip in exchange for pecuniary gain. The alternative advanced by the government—that intangible psychological benefits also qualify—is impermissibly vague and would give the government boundless discretion to prosecute the exchange of inside information. If accepted, the government's position would create a general duty to refrain from trading on material nonpublic information, despite this Court's repeated holdings that §10(b) imposes no such duty.

IV Salman's convictions should be reversed. Under the correct standard, the government had to prove that Maher tipped his brother Michael in exchange for some pecuniary benefit, and that Salman knew this. There was no evidence of any such pecuniary benefit motive, and thus nothing to know and no crime. Moreover, even if the Court were to adopt a broader definition of personal benefit, it should not extend the implied §10(b) tipping offense to a remote tippee who, like Salman, had no involvement in the insider's alleged fraudulent fiduciary breach.

ARGUMENT

Section 10(b) makes it illegal "for any person, directly or indirectly,...[t]o use or employ, in connection with the purchase or sale of any security...any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe...." 15 U.S.C. §78j(b). The statute does not address, much less proscribe, "insider trading." The Court, not Congress, created the tipping crime and established its elements, including the personal benefit requirement. In doing so, the Court made clear that "tippees" can trade on inside information unless the original tipper committed *fraud*.

The Court's precedents addressing both insider trading and fraud outside the securities context require the government to show that the tipper acted with intent to obtain money or property for himself. This narrow construction of the personal benefit element is also required because of

the judicial origins of the crime, due-process vagueness concerns, and the rule of lenity. Under an appropriately limited definition of the personal benefit element, Salman did not commit any crime.

I. SECTION 10(B) DOES NOT EXPRESSLY BAN INSIDER TRADING, AND THE COURT HAS CAREFULLY LIMITED THE IMPLIED "TIPPING" CRIME

A. Section 10(b) prohibits only the use of "manipulative or deceptive device[s] or contrivance[s]" in connection with the purchase or sale of securities, in violation of any applicable SEC regulations. It contains no language about "tipping" or insider trading.

Notably, Congress was aware of concerns regarding insider trading when it enacted the Exchange Act.[4] But it elected not to criminalize insider trading in §10(b). Instead, Congress chose to proscribe only a narrow category of insider trading, short-swing profits by certain corporate insiders, and to provide only a private civil remedy for its violation. *See* 15 U.S.C. §78p(b); *see also* STEPHEN M. BAINBRIDGE, SECURITIES LAW: INSIDER TRADING 26-27 (2d ed. 2007) (legislative history of §10(b) shows Congress did not intend "to create a sweeping prohibition of insider trading"). Congress also rejected the idea of tippee liability in that context. *See Blau v. Lehman*, 368 U.S. 403, 411-12 (1962). This shows that Congress did not intend for §10(b) to

[4] *See, e.g.*, Donald C. Cook & Myer Feldman, *Insider Trading Under the Securities Exchange Act*, 66 HARV. L. REV. 385, 386 (1953).

be an anti-insider-trading rule. "'[W]here Congress includes particular language in one section of a statute but omits it in another section of the same Act, it is generally presumed that Congress acts intentionally and purposely in the disparate inclusion or exclusion.'" *Russello v. United States*, 464 U.S. 16, 23 (1983) (citation omitted).

If the Court were inclined to reconsider its prior cases, it could readily hold, based on the plain language of the statute, that §10(b) does not prohibit insider trading at all—at least in the usual case where transactions are conducted anonymously in public markets, with no interaction with or deception of a counterparty. As Justice Scalia observed, "the unelaborated statutory language: '[t]o use or employ, in connection with the purchase or sale of any security...any manipulative or deceptive device or contrivance,' §10(b), must be construed to require the manipulation or deception of a party to a securities transaction." *United States v. O'Hagan*, 521 U.S. 642, 679 (1997) (concurring in part and dissenting in part). Commentators have recognized that "insider trading in no way resembles deceit.[5] No representation is made, nor is there any reliance, change of position, or causal connection between the defendant's act and the plaintiff's losses." Michael P. Dooley, *Enforcement of Insider Trading Restrictions*, 66 VA. L. REV 1, 59 (1980). Moreover, since insider trading is not deceptive, and thus not expressly

[5] "Manipulat[ion]" is a term of art irrelevant here. It refers to "practices, such as wash sales, matched orders, or rigged prices, that are intended to mislead investors by artificially affecting market activity." *Santa Fe Indus., Inc. v. Green*, 430 U.S. 462, 476 (1977).

prohibited by the statute, it would be unconstitutional for the Court to create an insider trading crime. *See, e.g.*, *Welch v. United States*, 136 S. Ct. 1257, 1268 (2016) ("separation of powers prohibits a court from imposing criminal punishment beyond what Congress meant to enact") *Bousley*, 523 U.S. at 620-21, *United States v. Hudson*, 7 Cranch 32, 34 (1812) (federal courts lack power to create common-law crimes; "[t]he legislative authority of the Union must first make an act a crime, affix a punishment to it, and declare the Court that shall have jurisdiction of the offence"); *cf.* John C. Coffee, Jr., *The 'Tip' of the Bunny's Nose: Sniffing Out Crime Where None Exists*, LEGAL TIMES, Sept. 25, 1989, at 34, 35 ("law of insider trading is developing through after-the-fact judicial decision-making," which "inevitably leads to the criminal law's overexpansion" and violates separation of powers).

Furthermore, even though §10(b) defers to the SEC to define "manipulative or deceptive" conduct, the agency has never used its rulemaking authority to ban insider trading. Rule 10b–5 is a general anti-fraud provision, but it does not mention insider trading and encompasses only conduct already prohibited by §10(b). *See O'Hagan*, 521 U.S. at 651.[6] Although the SEC has promulgated two §10(b) insider trading rules, they do not address the personal benefit requirement and expressly defer to

[6] Similar to §10(b), Rule 10b–5 makes it unlawful to "employ any device, scheme or artifice to defraud," make a false statement or misleading omission, or "engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person." 17 C.F.R. §240.10b–5.

the courts to define this aspect of insider trading law. 17 C.F.R. §240.10b5–1 prelim. n. (disclaiming any intention to "modify the scope of insider trading law" which is "otherwise defined by judicial opinions"); 17 C.F.R. §240.10b5–2 prelim. n. (same). Consequently, the source of §10(b)'s limited ban on insider trading is entirely judicial.

B. This Court first addressed whether insider trading can violate §10(b) in *Chiarella v. United States*, 445 U.S. 222 (1980). The defendant was an employee of a financial printer who prepared printing announcements for corporate takeover bids. He deduced the identities of target companies before the announcements were released and, without disclosing that information, purchased shares in those companies, which he sold immediately after the takeover bids were made public. *Id.* at 224.

The issue presented was whether the employee violated §10(b) by failing to inform sellers that he knew of a forthcoming takeover bid. The government argued that the defendant was guilty so long as he used material nonpublic information while knowing that others trading in the market did not have access to the same information. This Court rejected the government's theory and refused to "recogniz[e] a general duty...to forgo actions based on material, nonpublic information." *Id.* at 233. Such a broad duty would "depart[] radically from the established doctrine that duty arises from a specific relationship between two parties." *Id.* The Court held that it could not adopt such a duty "absent some explicit evidence of congressional intent" to prohibit

all trading on nonpublic information, which did not exist. *Id.*

In fact, neither the statute nor its legislative history provided any "specific guidance" on whether insider trading can violate §10(b). *Id.* at 226. Relying principally on *Cady, Roberts & Co.*, 40 S.E.C. 907 (1961), an administrative opinion in a case that was settled, the Court held that corporate insiders who have material nonpublic information owe a duty to their shareholders to disclose the information before trading or else abstain from trading. 445 U.S. at 227-30.

But the Court stressed that §10(b) is an anti-*fraud* provision, and "not every instance of financial unfairness constitutes fraudulent activity under §10(b)." *Id.* at 232. Emphasizing prior precedents requiring §10(b) to be construed narrowly, the Court explained that the statute "is aptly described as a catchall provision, but what it catches must be fraud." *Id.* at 234-35. "When an allegation of fraud is based upon nondisclosure, there can be no fraud absent a duty to speak." *Id.* at 235. Thus, "silence in connection with the purchase or sale of securities may operate as a fraud actionable under §10(b)," but only where there is "a duty to disclose arising from a relationship of trust and confidence between parties to a transaction." *Id.* at 230; *see also id.* at 235 ("We hold that a duty to disclose under §10(b) does not arise from the mere possession of nonpublic market information."). The Court thus held that the judicially-implied insider trading offense applies only where the person who trades has a fiduciary relationship with the issuer of the securities.

Because the defendant was not a corporate insider and received no confidential information from the target company, the Court held that he had no such fiduciary duty, and his conviction must be reversed. *Id.* at 231-33.

Three years later, in *Dirks*, the Court addressed tippee liability. Dirks was a securities analyst at a broker-dealer. He received material nonpublic information from Secrist, an insider at a life insurance company, who indicated that the company's assets were vastly overstated. Secrist tipped Dirks so that he could expose the fraud. Dirks relayed this information to clients and investors who sold their stock, thereby avoiding losses when the company's fraud became known and its stock price plummeted. The SEC sued Dirks, alleging that he had aided and abetted securities fraud by relaying material nonpublic information to people who traded the stock. 463 U.S. at 650-51.

This Court held that Dirks did not violate §10(b). The Court once again rejected the SEC's theory "that the antifraud provisions require equal information among all traders" as "inconsistent with congressional intent," and reaffirmed its holding in *Chiarella* that there is no general duty to refrain from insider trading. *Id.* at 656-57. The "disclose-or-refrain duty is *extraordinary*," and must be limited; "only some persons, under some circumstances, will be barred from trading while in possession of material nonpublic information." *Id.* at 657 (emphasis added; quotation marks omitted).

One of the Court's reasons for limiting the scope of §10(b) insider trading liability was that the free flow of information is essential to the fairness of the securities markets, and a strict ban on insider trading could over-deter the legitimate exchange of information and undermine the integrity of the marketplace. *Id.* at 658; *see also* Selective Disclosure & Insider Trading, Exchange Act Release No. 43154, 65 Fed. Reg. 51716-01, 51722 (Aug. 24, 2000) ("Analysts can provide a valuable service in sifting through and extracting information that would not be significant to the ordinary investor to reach material conclusions."); Andrew N. Vollmer, *How Hedge Fund Advisers Can Reduce Insider Trading Risk*, 3 J. SEC. L., REG. & COMPLIANCE 106, 107-08, 111-12 (2010) (describing the "variety of legitimate reasons" that analysts have "for communicating privately with the senior management of a public company").[7]

The Court held that a tippee is not liable "whenever he receives inside information from an insider," because a tippee generally owes no duty to the corporation's shareholders. *Dirks*, 463 U.S. at 655-56. However, a tippee who trades on inside information can violate §10(b) if the insider breached his fiduciary duty by disclosing the information, and the tippee knew that. *Id.* at 659-60. In this

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[7] Many scholars argue that a broad prohibition on insider trading can harm the securities markets. *See, e.g.*, Henry G. Manne, *The Case for Insider Trading*, WALL ST. J., Mar. 17, 2003; FRANK H. EASTERBROOK & DANIEL R. FISCHEL, THE ECONOMIC STRUCTURE OF CORPORATE LAW 256-59 (1991); Dennis W. Carlton & Daniel R. Fischel, *The Regulation of Insider Trading*, 35 STAN. L. REV. 857, 861-82 (1983).

situation, the tippee is considered derivatively liable for the insider's breach of duty. *See id.* at 659-60.

"Not 'all breaches of fiduciary duty in connection with a securities transaction,' however, come within the ambit of [§10(b) and] Rule 10b–5. There must also be 'manipulation or deception.'" *Id.* at 654 (quoting *Santa Fe Indus. v. Green*, 430 U.S. 462, 472 (1977)). The Court held that the particular type of fiduciary breach that could be deceptive within the meaning of §10(b) is an insider's exploitation of corporate information for his own personal "benefit" or "gain." "Absent some *personal gain*" by the corporate insider, neither the insider nor the alleged tippee violates §10(b). 463 U.S at 662 (emphasis added). Insiders are "forbidden by their fiduciary relationship from personally using undisclosed corporate information to their advantage, [and] they may not give such information to an outsider for the same improper purpose of *exploiting* the information for their [*i.e.*, the insiders'] *personal gain*." *Id.* at 659 (emphasis added).

II. BENEFIT MEANS PECUNIARY GAIN UNDER THE COURT'S INSIDER TRADING AND FRAUD PRECEDENTS

The *Dirks* Court explained that the purpose of the personal benefit rule is to provide a "guiding principle" for market participants who daily encounter and transmit rumors, information and analysis. 463 U.S. at 664. Otherwise they would be "forced to rely on the reasonableness of the SEC's litigation strategy," a "hazardous" endeavor. *Id.* at

664 n.24. Consistent with that goal of providing a "guiding principle," the Court emphasized that the test for determining whether an insider sought a personal benefit should not require the government or the courts to "to read the parties' minds." *Id.* at 663. Rather, the test "focus[es] on objective criteria, *i.e.*, whether the insider receives a direct or indirect personal benefit from the disclosure, such as a pecuniary gain or a reputational benefit that will translate into future earnings." *Id.*

The Court cited "cash, reciprocal information, or other things of value" as specific examples of benefits that would meet its test. *Id.* at 664 (citation omitted); *see also id.* at 654 (explaining that insider commits fraud "only where he fails to disclose material nonpublic information before trading on it and thus makes 'secret *profits*.'") (quoting *Cady, Roberts*, 40 S.E.C. at 916 n.31) (emphasis added). These examples, the Court's use of terms such as "gain" synonymously with "benefit," and its focus on insiders who "exploit" corporate information for "profit" show that it was principally concerned with situations in which the insider tips for pecuniary gain. The term "gain" connotes the improper use of corporate information to obtain something concrete, tangible and pecuniary. *See, e.g.*, BLACK'S LAW DICTIONARY 792 (10th ed. 2014) (defining "gain" as "[a]n increase in amount, degree, or value" and "[e]xcess of receipts over expenditures or of sale price over cost").

The Court identified "objective facts and circumstances that often justify" an inference of an insider's breach of duty. *Id.* at 664. The first is a

"quid pro quo" relationship between the insider and the tippee—in other words, a situation in which the insider is receiving something in return for the information. *Id.* But the Court also suggested that an insider's "intention to benefit" the tippee or "gift of confidential information to a trading relative or friend," where the "tip and trade resemble trading by the insider himself followed by a gift of profits to the recipient," might permit an inference of a fiduciary breach violating §10(b). *Id.*

As explained below, this language should not be read to allow a finding of personal benefit where the "benefit" is, at most, psychological and not pecuniary. The purpose of the test is to capture fraud by the insider, and this Court's precedents confirm that the core of fraud is the insider's exploitation of his position for personal profit, not for intangible benefits. Put another way, for tipping and trading on a "tip" to be fraudulent, the tipper's motive must be to obtain money or property for himself.

A. Insider Trading Precedents

The Court's express purpose in recognizing a limited form of tipping liability was to capture situations where an insider improperly "exploits" confidential information for "personal gain" in a manner analogous to the improper exploitation by an insider who trades without disclosing the information. *See Dirks*, 463 U.S. at 659, 662. That is why *Dirks* repeatedly instructs that tipping is fraudulent only if there is some personal benefit to the insider, and uses "benefit" interchangeably with

terms like "gain" that connote tangible monetary profit. The examples the Court employed to illustrate the type of benefit that would suffice involved financial benefits such as "pecuniary gain," "future earnings," "cash, reciprocal information, or other things of value." *Id.* at 663-64.

The Court drew on administrative and lower-court decisions that similarly involved only tangible financial benefits to the tipper, further confirming its focus on monetary gain. In *Cady, Roberts*, for example, a director of a public company who was also a broker provided the company's confidential information to his partner so that they could engage in profitable trades in the firm's clients' accounts. 40 S.E.C. 907 at [*2] (cited in *Dirks, passim*). In *Ross v. Licht*, the insiders tipped others so they could share in the profits from a public resale of the stock the tippees would acquire. 263 F. Supp. 395, 401 (S.D.N.Y. 1967) (cited at 463 U.S. at 661 n.20). Similarly, in *Merrill Lynch, Pierce, Fenner & Smith, Inc.*, the tipper received commissions and compensation on trades executed by its customers. 43 S.E.C. 933 at [*2] (1968) (cited at 463 U.S. at 654, 655).

The *Dirks* Court's focus on the insider's profit motive accords with *Chiarella* and other insider trading cases recognizing that fraud turns on the defendant's pecuniary motive. For example, when the Court first held that insider trading could be fraud, it relied on prior administrative and judicial decisions that involved insiders who received actual, pecuniary benefits—profits from trading or other monetary rewards. *See Chiarella*, 445 U.S. at 227-

30. The Court cited *Cady, Roberts*, discussed *supra*; *SEC v. Texas Gulf Sulphur Co.*, 401 F.2d 833 (2d Cir. 1968), where the defendants made trading profits; and *Affiliated Ute Citizens v. United States*, 406 U.S. 128 (1972), where they earned commissions and gratuities.

Likewise, in *O'Hagan*, the fraudster acted for his own pecuniary benefit. There the Court recognized that misappropriation of confidential corporate information can be fraudulent under §10(b) when the misappropriator "trades on the information" and makes money ($4.3 million). 521 U.S. at 648, 663. Significantly, the *O'Hagan* Court confirmed that the reason the insider in *Dirks* had not violated §10(b) was that he "had acted not for personal profit," but to expose a fraud. *Id.* at 663.

Similarly, in *Carpenter v. United States*, 484 U.S. 19 (1987), the Court upheld mail and wire fraud convictions for insider trading because a *Wall Street Journal* writer exploited the *Journal*'s confidential information by leaking it to brokers who traded and gave the writer a share of the profits. The Court drew on sources including common-law fiduciary duty claims that can be brought to recover trading "'profits'" from a person who "'exploit[s]'" information acquired from his fiduciary "'for his own personal benefit.'" *Id.* at 27-28 (quoting *Diamond v. Oreamuno*, 24 N.Y.2d 494, 497 (1969)).

Pecuniary gain is also required in the short-swing profit insider trading statute discussed *supra* at 21, even though it is not a fraud provision. There, "profit" signifies "direct pecuniary benefit to the

insider." *CBI Indus., Inc. v. Horton*, 682 F.2d 643, 646 (7th Cir. 1982) (Posner, J.). In that context, a familial relationship is not a sufficient benefit: "[I]t is not enough that ties of affinity or consanguinity between the nominal recipient and the insider make it likely that the insider will experience an enhanced sense of well-being as a result of the receipt, or will be led to reduce his gift-giving to the recipient." *Id.* On the contrary, "[t]he standard of direct pecuniary benefit excludes by definition any attempt to monetize the emotional satisfaction that [a defendant] might derive from a transaction that increased the wealth of his sons." *Id.* at 647.

B. Analogous Crimes

The Court has emphasized tangible gain when construing federal fraud statutes outside the insider trading context as well. These cases, like the §10(b) insider trading cases, often present the question of when a person's breach of duty to the public or her employer can constitute criminal fraud. There, as here, criminality turns on whether the person has exploited her position for personal gain; the focus is money or property, not intangible "benefits."

For instance, in *McNally v. United States*, 483 U.S. 350 (1987), the Court construed the mail fraud statute, which prohibits fraudulent schemes to "obtain[] money or property." The Court held that such fraud was "limited in scope to the protection of property rights" and thus did not cover a state official's purported scheme to deprive the public of his "honest services." Then, in *Skilling v. United States*, the Court limited the scope of the ensuing

"honest services fraud" statute to cases involving a *quid pro quo* exchange for money, *i.e.*, "bribes or kickbacks." 561 U.S. 358, 407-09 (2010). The Court emphasized that such pecuniary exchanges were the "core" of the offense, in part because of similar statutes that also focused on public officials' misconduct-for-monetary-profit schemes. *See id.* at 412-13; *see also Cleveland v. United States*, 531 U.S. 12, 22-23 (2000) (false statements on state video poker license application not mail fraud because defendants did not obtain money or "economic" property through their deceit). And in the related context of Hobbs Act extortion, the Court has rejected the invitation to treat "abstract" benefits like a recommendation as "property" the defendant sought to obtain. *See Sekhar v. United States*, 133 S. Ct. 2720, 2726-27 (2013).

In short, under the Court's precedents, trading on a tip can only be fraud if the tipper's purpose was to obtain some pecuniary benefit.

C. This Case Does Not Involve Any Securities Fraud

The facts of this case are far afield from the fraudulent conduct the Court read §10(b), like other anti-fraud provisions, to cover. Maher did not trade on the information, and he did not provide it to get a kickback. On the contrary, Maher gained nothing of value from his disclosures, and had no financial motive. His motive was to get a bullying brother "off his back." Indeed, the government has conceded that Maher's "breaches of fiduciary duty were in large part the result of Michael Kara's persistence in

seeking inside information." Sentencing Mem. at 7, *United States v. Kara*, No. 09-cr-00417-EMC-1 (N.D. Cal. Dec. 15, 2014) (Dkt. No. 249). The government acknowledged that Maher had a "complicated relationship with his brother, clearly." JA.402. Their relationship involved love and trust, but Michael also manipulated and deceived Maher. In most instances Maher disclosed information to Michael either with the understanding that his brother would not trade on it and would keep it confidential—Michael swore "on his daughter's life" that he would not trade, JA.81—or because Michael pressured him into providing the information. Maher opposed trading on inside information and discouraged Michael from doing so. These facts could hardly be more remote from the type of corrupt exchange the *Dirks* Court found §10(b) to capture.

III. THE CONSTITUTION AND INTERPRETIVE PRINCIPLES REQUIRE LIMITING THE PERSONAL BENEFIT ELEMENT TO PECUNIARY GAIN

Equating "personal benefit" with pecuniary gain not only comports with the Court's precedents, but also is necessary because any broader standard would be unconstitutional and inconsistent with interpretive principles requiring a clear and circumscribed rule.

A. Longstanding Interpretive Principles Dictate A Narrow Construction Of The Personal Benefit Element

1. *Criminal laws must be interpreted strictly.* Separation of powers, due process, and the related rule of lenity compel a limiting construction because a willful violation of §10(b) is a crime. 15 U.S.C. §78ff(a).[8] First, as this Court has repeatedly held, "penal laws are to be construed strictly" because "[i]t is the legislature, not the Court, which is to define a crime, and ordain its punishment." *United States v. Wiltberger*, 18 U.S. 76, 95 (1820). Courts have no authority to "define new federal crimes." *Skilling*, 561 U.S. at 415 (Scalia, J., concurring in part and concurring in judgment) (citing *Hudson*, 7 Cranch at 34); *see also United States v. Oakland Cannabis Buyers' Coop.*, 532 U.S. 483, 490 (2001) ("federal crimes are defined by statute rather than by common law"); *Lewis v. United States*, 523 U.S. 155, 160 (1998) (federal courts cannot "supplement... statutory crimes through the use of the common law").

Second, it is a violation of the Due Process Clause to "tak[e] away someone's life, liberty, or property under a criminal law so vague that it fails to give ordinary people fair notice of the conduct it

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[8] When a statute has both civil and criminal applications, the Court "must interpret the statute consistently, whether we encounter its application in a criminal or noncriminal context," including by applying the rule of lenity to construe the statute narrowly. *Leocal v. Ashcroft*, 543 U.S. 1, 11 n.8 (2004); *see also Whitman v. United States*, 135 S. Ct. 352, 353-54 (2014) (Scalia, J., respecting denial of certiorari).

punishes, or so standardless that it invites arbitrary enforcement." *Johnson v. United States*, 135 S. Ct. 2551, 2556 (2015) (citing *Kolender v. Lawson*, 461 U.S. 352, 357-58 (1983)); *see also, e.g.*, *Skilling*, 561 U.S. at 402-03. The Court can sometimes save a statute that would otherwise be void for vagueness—and thus avoid the constitutional question—by interpreting it narrowly. *See, e.g.*, *Skilling*, 561 U.S. at 405. But the Court may not "rewrite" the statute in order to save it. *See id.* at 415, 423-24 (Scalia, J., concurring in part and concurring in judgment).

Third, to the extent there is any ambiguity about the meaning of the personal benefit requirement, such ambiguity "should be resolved in favor of lenity." *Cleveland*, 531 U.S. at 25 (quotation marks omitted); *see also, e.g.*, *Yates v. United States*, 135 S. Ct. 1074, 1088 (2015). "[T]his time-honored interpretive guideline serves to ensure both that there is fair warning of the boundaries of criminal conduct and that legislatures, not courts, define criminal liability." *Crandon v. United States*, 494 U.S. 152, 158 (1990) (quotation marks omitted). Given the absence of any applicable statutory text, the need for a lenient construction is even stronger here. After all, the basis for the rule of lenity is that "the power of punishment is vested in the legislative, not in the judicial department," and "the legislature, not the Court,...is to define a crime." *Wiltberger*, 18 U.S. at 95.

2. *Section 10(b) is narrowly interpreted even in civil cases, to avoid a separation-of-powers problem.* In its insider trading decisions, the Court has emphasized the need to construe §10(b)

narrowly, explaining that "the 1934 Act cannot be read more broadly than its language and the statutory scheme reasonably permit." *Chiarella*, 445 U.S. at 234 (quotation marks omitted); *see also O'Hagan*, 521 U.S. at 651. The Court has articulated a similar limiting principle in defining the scope of the §10(b) private civil action, which was judicially implied just like the insider trading offense. For instance, in *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723 (1975), the Court held that only purchasers or sellers of securities could bring private §10(b) suits. The Court reasoned that Congress "had little trouble in...expressly" providing a civil remedy in other provisions to those who neither purchase nor sell securities, but had not expressly done so in §10(b), and that the §10(b) private action should be circumscribed because it was "judicially[-created]." *Id.* at 734, 749.

Similarly, in *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164 (1994), the Court observed that "our cases considering the scope of conduct prohibited by §10(b) in private suits have emphasized adherence to the statutory language," and that the Court has "refused to allow 10b–5 challenges to conduct not prohibited by the text of the statute." *Id.* at 173. Because "[i]t is inconsistent with settled methodology in §10(b) cases to extend liability beyond the scope of conduct prohibited by the statutory text," and the text of §10(b) does not reach those who aid or abet a violation, the Court refused to recognize a private action for aiding and abetting. *Id.* at 177. Likewise, in *Janus Capital Group v. First Derivative Traders*, 564 U.S. 135 (2011), the Court emphasized the

"narrow scope" and "narrow dimensions" of the judicially implied §10(b) cause of action because "Congress did not authorize [it] when it first enacted the statute and did not expand [it] when it revisited the law." *Id.* at 142, 144 (refusing to extend §10(b) to defendant who was involved in but did not make false statements).

In *Stoneridge Investment Partners, LLC v. Scientific-Atlanta, Inc.*, 552 U.S. 148 (2008), the Court applied this narrow construction rule to reject private §10(b) "scheme liability." The Court explained that the limiting-construction rule in §10(b) cases is designed to avoid a constitutional separation-of-powers problem. The §10(b) private action "is a judicial construct that Congress did not enact in the text of the relevant statutes." 552 U.S. at 164. A limiting construction is thus required to avoid an exercise of power by the federal courts that "'conflicts with the authority of Congress under Art. III to set the limits of federal jurisdiction.'" *Id.* at 164-65 (citation omitted). "Concerns with the judicial creation of a private cause of action caution against its expansion....Though it remains the law, the §10(b) private right should not be extended beyond its present boundaries." *Id.* at 165.

These separation-of-powers concerns are implicated here too, because the insider trading offense, like the private §10(b) action, was created by the judiciary. *See* Andrew N. Vollmer, *A Rule of Construction for* Salman, Va. Pub. L. & Legal Theory Research Paper No. 28 (2016), *available at* http://ssrn.com/abstract=2749834. Indeed, these constitutional concerns are even more serious here

than in the civil context, because a person's liberty is at stake. *See Liparota v. United States*, 471 U.S. 419, 424 (1985) ("The definition of the elements of a criminal offense is entrusted to the legislature, particularly in the case of federal crimes, which are solely creatures of statute.").

B. The Ninth Circuit's Standard Is Indeterminate

If a gift or intention to benefit the tippee were enough to establish a personal benefit to the tipper, that would undermine the *Dirks* Court's desire to have a "limiting principle" to guide those "whose daily activities must be limited and instructed" by the insider trading rules, 463 U.S. at 664, as well as due process principles requiring fair notice discussed above.

By definition, a gift is intended to benefit the recipient; the giver neither receives nor typically expects a benefit in return. For example, the common-law meaning of "gift" is a voluntary transfer of property without consideration. *E.g.*, *Kehr v. Smith*, 87 U.S. 31, 34 (1873); BLACK'S LAW DICTIONARY 803 (10th ed. 2014) (defining gift as "voluntary transfer of property to another without compensation"). Likewise, under the tax code a gift "proceeds from a detached and disinterested generosity, out of affection, respect, admiration, charity or like impulses." *Comm'r v. Duberstein*, 363 U.S. 278, 285 (1960) (quotation marks and citation omitted). If giving something of value to another "proceeds primarily from...'the incentive of anticipated benefit' of an economic nature, it is not a

gift." *Id.* (quoting *Bogardus v. Comm'r*, 302 U.S. 34, 41 (1937)).

In arguing that a "gift" nevertheless qualifies as a benefit to the insider, the government presumably means to imply that the insider receives emotional satisfaction from giving the gift. But the insider will *always* have some kind of emotional response to the disclosure of corporate information. Which emotions give rise to insider trading liability, and which do not? The government has never answered this question, precisely because it wants to maximize its ability to punish insider trading regardless of whether the insider benefited in any concrete or tangible way. Any suggestion that the personal benefit requirement could be established by psychic gratification, such as the satisfaction derived from giving a gift, would render the requirement impermissibly vague. Such a malleable standard would be at odds with the due-process-based need for a bright line that "so clearly" advises market participants "in advance how to avoid an unlawful course of action." *M. Kraus & Bros. v. United States*, 327 U.S. 614, 621-22 (1946). It would also require traders, the courts, and the government to "read the parties' minds"—the precise uncertainty that the Court sought to avoid by focusing on "objective facts." *Dirks*, 463 U.S. at 663-64. Psychic reward necessarily turns on an inherently subjective inquiry, which fails to provide "an ascertainable standard of guilt." *United States v. L. Cohen Grocery Co.*, 255 U.S. 81 89 (1921). It should not be the touchstone for criminal liability.

In *Dirks*, for example, Secrist (the insider) likely obtained some personal satisfaction from exposing the fraud. One could plausibly argue that Secrist was giving a "gift" to Dirks when he disclosed that the company's assets were overstated, and when he allowed Dirks to expose the fraud, trade on the information, or tip others. After all, Secrist clearly knew that Dirks worked at a broker-dealer and would likely share the information with his investor-clients. *See* 463 U.S. at 648. But the Court found no benefit and no fraudulent fiduciary breach: "Under any objective standard, Secrist received no direct or indirect personal benefit from the disclosure." *Id.* at 666 n.27. Notably, the Court expressly rejected the notion that there is a fraud "whenever inside information is intentionally disclosed to securities traders." *Id.* It plainly would have reached the same result even if Secrist and Dirks had been relatives or friends. Under the Ninth Circuit's theory, by contrast, Secrist and Dirks would both be liable if they had had some personal relationship, since Secrist gave Dirks material nonpublic information knowing he would trade on it.

This case also illustrates how a standard that allows a finding of personal benefit based only on the parties' relationship can become a trap for the unwary. Any benefit Maher might have received is purely emotional, and it is unclear what that benefit could have been. His conduct resulted in anxiety, not psychic reward. If this qualifies as a "benefit" under the "gift" theory—as the government argued and the Ninth Circuit accepted—then virtually any disclosure of confidential information to a friend or relative could suffice, regardless of the tipper's

motive or whether the tipper obtains any concrete benefit from the exchange.

Cases involving remote tippees such as Salman also underscore the need for a clearer and more circumscribed definition of "personal benefit." A direct tippee is personally involved in the transfer of information and thus likely to be in a position to know the insider's motives. By contrast, a remote tippee often has no information about the tipper's motive. A remote tippee may know only the identity of and relationship between the parties, but nothing more. Because any benefit from making a gift is at best emotional or psychological and depends on the tipper's subjective state of mind, it will typically be impossible, especially for a remote tippee, to discern. What sort of relationship between the insider and the immediate tippee will suffice is also unclear. Where is the line between a "friend" and an acquaintance? Is an in-law a "relative"? If an insider's mother remarries after his father dies, is her new husband's child the insider's "relative"? Under the Ninth Circuit's indeterminate standard, ascertaining whether conduct falls within the statute's prohibited scope "devolv[es] into guesswork and intuition," triggering due-process vagueness concerns. *Johnson*, 135 S. Ct. at 2559.

This is a very real concern, because an insider's disclosure of confidential information to a friend or relative who might trade does not always reflect serious misconduct. There are many situations where insiders make such disclosures for innocent reasons or by mistake. For example, an insider might reveal corporate information to a

friend or relative inadvertently, *e.g.*, *Goetz*, SEC Litig. Release No. 21990, 2011 WL 2187726 (June 6, 2011); as part of his obligation to conduct due diligence for his employer, *e.g.*, *SEC v. Obus*, 693 F.3d 276, 290 (2d Cir. 2012); in managing family schedules ("I need to fly to Cupertino tomorrow for a work emergency"); or as occurred with some of the information here, to learn about scientific concepts relevant to his work or to contribute to discussions about a family member's medical problem, *supra* at 10.

As this Court has explained, securities law is "'an area that demands certainty and predictability.'" *Central Bank*, 511 U.S. at 188 (quoting *Pinter v. Dahl*, 486 U.S. 622, 652 (1988)). Congress and the SEC have committed volumes of legislation and regulations to ensuring that market actors understand the precise boundaries of permissible conduct.[9] Yet the government advocates a position that, if accepted, would render the most basic issue in securities law—whether a party may buy or sell a security—hopelessly vague. Particularly in complex regulatory regimes, however, rules "must be explicit and unambiguous in order to sustain a criminal prosecution." *M. Kraus & Bros.*, 327 U.S. at 621.

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[9] *See, e.g.*, 15 U.S.C. §77g, 17 C.F.R. §230.400 *et seq.* (registration statement requirements); 17 C.F.R. Part 229 (specifying nature and format of periodic disclosures issuers must make to investors); 17 C.F.R. §240.14a–1 *et seq.* (rules for proxy solicitations); 17 C.F.R. Part 243 (rules regarding selective disclosures).

C. The Ninth Circuit's Approach Unconstitutionally Delegates To Prosecutors The Power To Define The Crime

Using a "gift" concept as a proxy for the personal benefit element is also problematic because it fails to "'establish minimal guidelines to govern law enforcement'"—the most "important aspect of vagueness doctrine." *Kolender*, 461 U.S. at 358 (citation omitted). The *Dirks* Court sought to avoid a situation in which prosecutorial whim determines whether conduct is punishable. *See* 463 U.S. at 664 n.24 (holding that market participants should not be "forced to rely on the reasonableness of the [government's] litigation strategy"). Yet, in the three-plus decades since *Dirks*, the Department of Justice and the SEC have effectively nullified the personal benefit requirement by invoking the "gift" talisman whenever there is no tangible economic benefit to the tipper. *See generally* Stephen J. Crimmins, *Insider Trading: Where Is the Line?*, 2013 COLUM. BUS. L. REV. 330, 347 (2013). As a consequence, the personal benefit requirement, as applied, rarely presents a barrier to government action, even though trading on inside information is generally *not* illegal, and the *Dirks* Court sought to limit the scope of tip-based liability to "extraordinary" cases. 463 U.S. at 657.

1. *Pre-*Newman *overbreadth*. Until *Newman*, the lower courts typically rubber-stamped the government's watered-down version of the personal benefit requirement. Ignoring this Court's repeated holdings that there is no general duty to refrain from

trading on inside information, many lower courts have simply assumed that if an insider discloses material nonpublic information to an outsider this is enough to create an inference that the insider intended to benefit the tippee and thus to obtain some emotional or psychological benefit for himself. For example, the Seventh Circuit has concluded that "[a]bsent some legitimate reason for [the insider's] disclosure..., the inference that [his] disclosure was an improper gift of confidential corporation information is unassailable. After all, he did not have to make any disclosure, so why tell [the tippee] anything?" *SEC v. Maio*, 51 F.3d 623, 633 (7th Cir. 1995). *See also, e.g., SEC v. Blackwell*, 291 F. Supp. 2d 673, 692 (S.D. Ohio 2003) ("A mere allegation that the insider has disclosed material non-public information is sufficient to create a legal inference that the insider intended to provide a gift to the recipient of the information, thereby establishing the personal benefit requirement."); *SEC v. Blackman*, No. 3:99-1072, 2000 WL 868770, at *9 (M.D. Tenn. 2000) ("[T]he mere fact of [a tipper's] disclosure of... information sufficiently alleges a gift by him...so as to satisfy the personal benefit requirement of *Dirks*."); *SEC v. Rubin*, No. 91 Civ. 6531 (MBM), 1993 WL 405428, at *5 (S.D.N.Y. Oct. 8, 1993) (fact that tippee was tipper's broker was sufficient to create inference of personal benefit "absent evidence of an identifiable proper motive to disclose the information in question").

This approach turns on its head the Court's intention that the personal benefit test serve as a limiting principle to cabin §10(b) insider trading liability to extraordinary cases. A weak, ephemeral

standard invites prosecutors to abuse their power and risks exactly the discriminatory enforcement that the vagueness doctrine is designed to prevent, "raising the specter of potentially charging everybody...and seeing what sticks and who flips." *Ocasio v. United States*, No. 14-361, ---S. Ct.---, slip op. at 11 (May 2, 2016) (Sotomayor, J., dissenting).

That risk is not merely theoretical. In recent years the government has pursued an extremely aggressive litigation strategy to reduce the significance of the personal benefit requirement to virtually nil. The government has brought numerous prosecutions and enforcement actions where a tipper gratuitously provided information to a friend or relative. In those cases, there was no evidence that the tipper sought to profit from the tip, yet the government claimed a benefit solely because of the relationship between tipper and tippee. *See, e.g., United States v. Gansman*, 657 F.3d 85 (2d Cir. 2011) (extramarital affair); *United States v. Evans*, 486 F.3d 315 (7th Cir. 2007) (friends); *SEC v. Rocklage*, 470 F.3d 1 (1st Cir. 2006) (siblings); *SEC v. Warde*, 151 F.3d 42 (2d Cir. 1998) (friends); *United States v. Adcox*, CR A. NO. 15-00036-01, 2016 WL 616533 (W.D. La. Feb. 16, 2016) (brothers-in-law); *SEC v. Palermo*, No. 99 Civ. 10067(AGS), 2001 WL 1160612, at *7 (S.D.N.Y. Oct. 2, 2001) (friends). In many such instances, the tipper and tippee were not even close friends or relatives but mere casual acquaintances. *See, e.g., United States v. Cusimano*, 123 F.3d 83, 85 (2d Cir. 1997) ("subordinate and friend"); *SEC v. Maxwell*, 341 F. Supp. 2d 941 (S.D. Ohio 2004) (barber and customer); *United States v.*

ReBrook, 837 F Supp. 162 (S.D.W Va. 1993) ("acquaintances").

The government has also cast a wide net, pursuing remote tippees who have no relationship with the original tipper. For instance, in *SEC v. Conradt*, the SEC did not allege that the remote tippee knew the original source of the information, "let alone knew that the [source and the initial tippee] had a relationship of trust and confidence or that [the tipper] had obtained the information in breach of that relationship." 947 F. Supp. 2d 406, 412 (S.D.N.Y. 2013). *See also, e.g., United States v. McDermott*, 245 F.3d 133, 136 (2d Cir. 2001) (remote tippee received information through girlfriend, who was having affair with another man); *SEC v. Sargent*, 229 F.3d 68, 72-73 (1st Cir. 2000) (remote tippee received information from tipper's dentist). The *Newman* case is a paradigmatic example. The original tippers were insiders at two companies; one provided information to an acquaintance from college, supposedly to get "career advice," and the other gave it to a friend at church. The tippee-defendants were hedge fund managers who received the information fourth- or fifth-hand, only after it had passed through several intermediaries; the tippee-defendants did not know who the insiders were or why they had disclosed the information. Yet until their convictions were overturned by the Second Circuit, these defendants faced lengthy prison terms of 4½ and 6½ years. 773 F.3d at 444.

2. *The failed role of scienter.* The scienter requirement does not alleviate the vagueness problems caused by such an overbroad personal

benefit requirement. *Cf. O'Hagan*, 521 U.S. at 665-66 (rejecting vagueness attack on misappropriation theory of insider trading due to "sturdy safeguards Congress has provided regarding scienter"). To establish criminal liability, the government must prove that the defendant "willfully" violated §10(b). *See* 15 U.S.C. §78ff(a). This requires the government to prove "that the defendant acted with knowledge that his conduct was unlawful." *Bryan v. United States*, 524 U.S. 184, 191-92 (1998) (citing *Ratzlaf v. United States*, 510 U.S. 135, 137 (1994)); *see also Safeco Ins. Co. v. Burr*, 551 U.S. 47, 57 n.9 (2007) (as used in criminal statutes, "willfully" "limit[s] liability to knowing violations," *i.e.*, requiring defendant's "'knowledge that his conduct was unlawful'") (citation omitted).

However, the Ninth Circuit has gutted this safeguard against government overreaching by holding that mere recklessness can support *criminal* liability for securities fraud. *See United States v. Tarallo*, 380 F.3d 1174, 1188-90 (9th Cir. 2004).[10] The Ninth Circuit's application of the "willful blindness" doctrine also effectively reduces the knowledge-of-personal-benefit element of the crime to a mere negligence standard. This Court has held that willful blindness can establish actual knowledge only if the government shows that the defendant believes that there is "a high probability that a fact exists" and "take[s] deliberate actions to avoid

[10] The district court thus specifically instructed Salman's jury that "[a]cting willfully does not require that the defendant know that the conduct was unlawful"; [t]he government is not required to prove that the defendant knew that his acts were unlawful." Pet.App.56.

learning of that fact." *Global-Tech Appliances, Inc. v. SEB, S.A.*, 563 U.S. 754, 769 (2011). Yet the Ninth Circuit does not require any "deliberate actions" and instead held that merely showing that "a reasonable person would make further inquiries" suffices. Pet.App.24.

Particularly for remote tippees, the weak scienter standard solidifies the government's ability to bring charges as if the law created a general duty to refrain from trading on material nonpublic information, even though it does not. Under the Ninth Circuit standard, anyone who learns inside information has an affirmative duty to investigate who was the source of the information and what his motive for disclosing it was, or risk imprisonment.

This problem is further compounded by the government's repeated efforts to avoid even having to prove scienter. For example, it argued in *Newman* that a defendant may be convicted of insider trading even if the defendant did not know that the information was disclosed by an insider for personal benefit. The Second Circuit disagreed, in light of this Court's reasoning in *Dirks* and its well-settled precedents requiring the government to prove defendants' knowledge of the facts that make their conduct criminal. *Newman*, 773 F.3d at 447-51. But then the government took a different tack, attempting to dilute the knowledge requirement. The government maintained in its petitions for rehearing en banc and certiorari that knowledge of facts like the specificity of the information, its apparently nonpublic nature, or that it came from an insider is sufficient to prove a personal benefit—even

though none of this "proof" shows whether or how the insider actually benefited. *See, e.g.*, Pet. for Writ of Cert., *United States v. Newman*, No. 15-137, at 31 (arguing that remote tippees "at least consciously avoided confirming" that "detailed pre-announcement earnings-related information" was "disclosed by insiders for personal advantage"). The government has made similar arguments in other cases, even in the Second Circuit post-*Newman*. *See, e.g.*, SEC Mem. at 18, *SEC v. Payton*, 14 Civ. 4644 (S.D.N.Y. Aug. 24, 2015) (Dkt. No. 60); Gov't Mem. at 21-22, *United States v. Kimelman*, 10 Cr. 0056 (S.D.N.Y. May 4, 2015) (Dkt. No. 340); SEC Mem. at 12-13, *SEC v. Jafar*, 13 Civ. 4645 (S.D.N.Y. Feb. 13, 2015) (Dkt. No. 93).

Not surprisingly, then, most defendants confronted with insider trading charges feel they have no choice but to plead guilty or settle, no matter how thin the evidence of personal benefit might be. The reasons for this include the immense costs of litigation, the lower courts' frequent acquiescence in the government's overreaching, and the draconian potential prison sentences for insider trading. *See, e.g.*, Sentencing Tr. at 45, 49, *United States v. Riley*, 13 Cr. 339 (S.D.N.Y. Apr. 27, 2015) (78-month sentence for defendant-tipper whose personal gain was characterized by district court as "peanuts" and "essentially nothing"); Judgment, *United States v. Skowron*, 11 Cr. 699 (S.D.N.Y. Nov. 22, 2011) (Dkt. No. 27) (60-month sentence for tippee who pled guilty); Judgment, *United States v. Drimal*, 10 Cr. 056 (S.D.N.Y. Aug. 31, 2011) (Dkt. No. 261) (66-month sentence for remote tippee who pled guilty); Judgment, *United States v. Contorinis*, 09

Cr. 1083 (S.D.N.Y. Dec. 22, 2010) (Dkt. No. 94) (72-month sentence for tippee); *see generally* Jed S. Rakoff, *Why Innocent People Plead Guilty*, N.Y. REV. BOOKS (Nov. 20, 2014) (arguing that Sentencing Guidelines, although no longer mandatory, "provide prosecutors with weapons to bludgeon defendants into effectively coerced plea bargains"). Indeed, six defendants facing charges in connection with the *Newman* case pleaded guilty and cooperated to avoid long prison sentences, even though the government was later forced to concede their innocence and consent to withdrawal of their pleas in light of the Second Circuit's ruling. *See* Statement of U.S. Attorney Preet Bharara (Oct. 22, 2015), https://www.justice.gov/usao-sdny/pr/statement-us-attorney-preet-bharara-dismissal-charges-against-michael-steinberg-and-six.

3. *The de facto standard is now the "parity-of-information" rule that this Court repeatedly rejected.* With only a vague personal benefit requirement, the government has effectively usurped the power to define the §10(b) insider trading violation. Before *Newman*, the personal benefit element had been reduced to a meaningless peppercorn, subverting this Court's careful efforts to limit the tipping violation. As the *Newman* court observed, the personal benefit standard "does not suggest that the Government may prove the receipt of a personal benefit by the mere fact of a friendship, particularly of a casual or social nature. If that were true, and the Government was allowed to meet its burden by proving that two individuals were alumni of the same school or attended the same church, the

personal benefit requirement would be a nullity." 773 F.3d at 452.[11]

The government's overreaching has defeated the *Dirks* Court's goal of limiting the disclose-or-refrain duty to "extraordinary" situations that are clearly delineated. In the present environment, market participants who are merely exposed to material nonpublic information trade at their peril. The *de facto* rule is therefore not the law articulated by this Court, but instead the "parity-of-information" rule that the Court has repeatedly rejected. Responsible market participants cannot ignore the risk of overzealous prosecutions even in instances where there is no objective evidence of personal benefit. This situation has resulted in precisely the arbitrary and discriminatory enforcement the Due Process Clause is designed to prevent. *See Kolender*, 461 U.S. at 358 (warning of dangers caused by vague criminal statutes that "may permit 'a standardless sweep [that] allows policemen, prosecutors, and juries to pursue their personal predilections'") (citation omitted); *Papachristou v. City of Jacksonville*, 405 U.S. 156, 170 (1972) (same).

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[11] As one noted securities-law scholar observed, *Newman* "finally put a judicial cap on" the government's "quest to expand the definition of insider trading to capture virtually every information asymmetry and the virtual presumption of guilt" in its press releases. Stephen Bainbridge, *US v Newman: A Big Win for Coherence and Fairness in Insider Trading Law*, PROFESSORBAINBRIDGE.COM (Dec. 11, 2014), http://www.professorbainbridge.com/professorbainbridgecom/2014/12/us-v-newman-a-big-win-for-coherence-and-fairness-in-insider-trading-law.html.

Even if a broad ban on tippee trading were the best policy, that is for Congress, and not the courts, much less the prosecutors, to determine. "The role of this Court is to apply the statute as it is written—even if [it] thinks some other approach might 'accor[d] with good policy.'" *Burrage v. United States*, 134 S. Ct. 881, 892 (2014) (quoting *Comm'r v. Lundy*, 516 U.S. 235, 252 (1996)). *See also United States v. Santos*, 553 U.S. 507, 523 (2008) ("[E]ven if ...statutory ambiguity 'effectively' licenses us to write a brand-new law, we cannot accept that power in a criminal case, where the law must be written by Congress.") (plurality opinion). As Justice Scalia observed: "Deferring to the prosecution branch's expansive views of [statutes like §10(b)] 'would turn [their] normal construction...upside-down, replacing the doctrine of lenity with a doctrine of severity.'" *Whitman v. United States*, 135 S. Ct. 352, 353 (2014) (Scalia, J., respecting denial of certiorari) (citation omitted).

Congress has not seen fit to ban insider trading or codify a parity-of-information rule, so it is often perfectly legal to trade on material nonpublic information.[12] "To punish a person because he has

[12] One reason for this may be that there are other mechanisms to deter the illicit disclosure of inside information. For instance, the SEC's Regulation FD prohibits issuers and certain of their personnel from making selective disclosures to investment professionals, 17 C.F.R. §243.100; state law remedies may be available for shareholders to assert claims based on insider trading, DONALD C. LANGEVOORT, 18 INSIDER TRADING REGULATION, ENFORCEMENT, & PREVENTION §10:12 (2016); by statute, broker-dealers must maintain and enforce written policies "to prevent the misuse...of material, nonpublic information by such broker or dealer or any person associated

done what the law plainly allows him to do is a due process violation of the most basic sort." *Bordenkircher v. Hayes*, 434 U.S. 357, 363 (1978). Until Congress bans all insider trading, market participants have a right to a clear line so that they can trade, even based on inside information, when doing so is legal, rather than being forced to avoid engaging in legal activity because the standard is malleable and subject to manipulation by zealous government officials. This is true regardless of whether insider trading violates ethical or moral norms. *See, e.g., Skilling*, 561 U.S. at 410 (failure to disclose conflict of interest does not violate criminal honest services fraud statute); Coffee, *supra*, at 35 ("To realize the criminal law's normative goal, people must be able to arrange their affairs to avoid entanglement with the criminal law.") (citing HERBERT L. PACKER, THE LIMITS OF THE CRIMINAL SANCTION (1968)).[13]

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with such broker or dealer," 15 U.S.C. §78*o*(g); and companies typically maintain internal policies and procedures to prevent insider trading, as was the case here, Langevoort, *supra*, §12.6. There is no reason to think these other measures are inadequate; criminal punishment should be reserved for egregious misconduct, not basic regulation of the securities markets.

[13] There is no societal consensus that insider trading is inherently wrongful. *See, e.g.*, John P. Anderson, *Greed, Envy, and the Criminalization of Insider Trading*, 2014 UTAH L. REV. 1 (2014); Jonathan R. Macey, *Ethics, Economics, and Insider Trading: Ayn Rand Meets the Theory of the Firm*, 11 HARV. J.L. & PUB. POL'Y 785 (1988). Indeed, the Second Circuit has required a higher level of scienter in insider trading cases

* * *

In sum, a pecuniary benefit is the paradigmatic benefit described not only in *Dirks*, but also in this Court's other insider trading cases, the lower-court and administrative decisions that the Court relied on to create the insider trading §10(b) offense, and the Court's decisions holding that other fraud offenses require a showing that the fraudster acted to obtain money or property. Constitutional principles also demand that *Dirks*' personal benefit requirement be limited to pecuniary gain. That interpretation avoids the inherent vagueness of reading *Dirks*' "gift" language too broadly, as well as the attendant separation-of-powers concerns. *See generally Burrage*, 134 S. Ct. at 891 ("Especially in the interpretation of a criminal statute subject to the rule of lenity, we cannot give the text a meaning that is different from its ordinary, accepted meaning, and that disfavors the defendant.") (citation omitted).

As Judge Easterbrook pointed out when reversing an honest services fraud conviction based on a similarly amorphous benefit theory: "It is linguistically *possible* to understand 'private gain' as

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(continued...)

(knowledge of "unlawfulness") than in prosecutions for "deliberately mislead[ing] investors about a security" (only knowledge of "wrongfulness" is required), even though "willfulness" is the standard in both contexts. "Unlike securities fraud, insider trading does not necessarily involve deception, and it is easy to imagine an insider trader who receives a tip and is unaware that his conduct was illegal and therefore wrongful." *United States v. Kaiser*, 609 F.3d 556, 569 (2d Cir. 2010); *accord Newman*, 773 F.3d at 450.

whatever adds to the employee's income or psyche—anything the employee would pay to have, rather than pay to avoid—but the Rule of Lenity counsels us not to read criminal statutes for everything they can be worth." *United States v. Thompson*, 484 F.3d 877, 884 (7th Cir. 2007). The prohibited gain must "come[] from third parties who suborn the employee with side payments." *Id.* Employees might breach their fiduciary duties for "psychic benefit[s]" such as "friendship" or the "approbation" of others, but these are simply not "the sort of 'private gain' that makes an act criminal under" the honest services fraud statute. *Id.* Nor should such psychic benefits make tipping by a corporate insider, or trading on that insider's tip, criminal securities fraud.

IV. THE COURT SHOULD REVERSE SALMAN'S CONVICTIONS

No reasonable juror could find Salman guilty beyond a reasonable doubt.

A. Application of the principles set forth above requires reversal of Salman's conviction. It is undisputed that Maher received no pecuniary gain in exchange for disclosing the information to Michael. This was confirmed by the district court and the SEC in related proceedings. *See supra* at 5. Accordingly, Maher did not commit securities fraud, and Salman was free to trade on the information: "[T]he tippee's duty to disclose or abstain is derivative from that of the insider's duty"; "[a]bsent a breach by the insider, there is no derivative breach," and thus no violation of §10(b) by anyone. *Dirks*, 463 U.S. at 659, 662.

Moreover, the government had to prove not only that Maher received a pecuniary benefit (which it could not prove), but also Salman's knowledge of such a benefit, because the defendant must be aware of the facts that supposedly make his conduct criminal. *See, e.g., Staples v. United States*, 511 U.S. 600, 605 (1994). *Dirks* requires proof that the tippee "knowingly participate[d]" in the insider's fraudulent fiduciary breach. 463 U.S. at 659-60; *see Newman*, 773 F.3d at 447-50. Since there was no pecuniary benefit, there was nothing for Salman to know.

Nor can the conspiracy count save the conviction. Conspiracy is an agreement "to commit an[] offense against the United States." 18 U.S.C. §371. If the personal benefit test requires proof that the insider disclosed information in exchange for pecuniary gain, there was no offense against the United States, since Maher undisputedly neither sought nor obtained any pecuniary gain. A conspiracy conviction cannot stand if the alleged object of the conspiracy was not a crime. *Parr v. United States*, 363 U.S. 370, 393 (1960); *see also Ocasio*, slip op. at 5 ("conspiracy is a joint commitment to an 'endeavor which, if completed, would satisfy all of the elements of [the underlying substantive] criminal offense'") (brackets in original; citation omitted).

B. Even if the Court does not adopt the pecuniary gain standard for the personal benefit requirement, it should reverse Salman's conviction, because he had no involvement, directly or indirectly, in any breach of fiduciary duty by Maher. Unlike Maher, Salman had no duty to Citigroup or

its clients. Unlike Michael, he did not induce or participate in any way in inducing Maher's disclosures to Michael. He did not aid and abet or conspire with Maher, who never suspected that his brother was relaying information to others. JA.131. In fact, any crime Maher committed was complete *before* Salman learned of the information, when Michael traded on the information for his own account. *See* JA.262-63, 276.

Section 10(b) should not be applied to remote tippees who do not directly participate in the insider's breach of duty or substantially assist a tippee who does. The statute only proscribes deception and manipulation. The theory in the case law is that some insider trading is covered because it amounts to deception in violation of a fiduciary duty to the securities issuer and its shareholders, not the investing public. *Dirks*, 463 U.S. at 654; *Chiarella*, 445 U.S. at 227-28; *cf. O'Hagan*, 521 U.S. at 652 (misappropriation involves breach of duty to source of information). But Salman did not *deceive* anyone. He made no false statements in connection with his trades; he had no duty to the issuers or their shareholders that could have made his silence deceptive. *See Chiarella*, 445 U.S. at 227-28.

This Court has never considered the potential liability of a remote tippee like Salman, and the *Dirks* Court never suggested that remote tippees who did not participate in the tipper's breach would be liable. On the contrary, the Court said there was a need for a ban on only "some tippee trading," and emphasized that the duty to refrain or disclose was "extraordinary." 463 U.S. at 657, 659. In explaining

who was covered, the Court held that "the transactions of those *who knowingly participate with the fiduciary in such a* breach are 'as forbidden' as transactions 'on behalf of the trustee himself.'" *Id.* (emphasis added; citation omitted). This suggests direct participation, as occurs with the immediate tippee, and belies any intent to cover anyone downstream who later receives the information. *See also* Donald C. Langevoort, *Insider Trading and the Fiduciary Principle: A Post-*Chiarella *Restatement*, 70 CAL. L. REV. 1, 28 (1982) (*Chiarella* "require[es] some co-venture between the tipper and tippee before that breach can be attributed to the nonfiduciary tippee," which "suggests a very narrow class of tippee-trading cases that fall within the prohibition").

The Court should therefore decline to extend the judge-made tipping crime to remote tippees like Salman—just as the Court refused to expand the scope of the private §10(b) action in *Blue Chip Stamps*, *Central Bank*, and their progeny. *See, e.g.*, *Central Bank*, 511 U.S. at 177-78 (Court cannot "amend [§10(b)] to create liability for acts that are not themselves manipulative or deceptive within the meaning of the statute"); *Halliburton Co. v. Erica P. John Fund, Inc.*, 134 S. Ct. 2398, 2411 (2014) (Court "'must give 'narrow dimensions...to a right of action Congress did not authorize when it first enacted the statute and did not expand when it revisited the law.'") (citations omitted); *Amgen Inc. v. Conn. Ret. Plans & Trust Funds*, 133 S. Ct. 1184, 1202 (2013) ("We have no warrant to encumber securities-fraud litigation by adopting an atextual requirement...that

Congress, despite its extensive involvement in the securities field, has not sanctioned.").

This case well illustrates how expanding the implied tipping crime can lead to incongruous results that defy the theoretical underpinings of tippee liability. Because the tippee's duty and liability are "solely derivative" of the insider's, a tippee cannot "be said to be as culpable as one whose breach of duty gave rise to that liability in the first place." *Bateman Eichler, Hill Richards, Inc. v. Berner*, 472 U.S. 299, 312-13 (1985). The tipper is always most culpable because the tipper's conduct causes the violation. *See Dirks*, 463 U.S. at 659. *See also id.* n.23 (tippers are "'most directly culpable in a violation'") (citation omitted). Both the SEC and the district court found that the tipper here was not very culpable and deserved lenience. *See supra* at 5. Under the theory of derivative liability, Salman was necessarily even less culpable. Yet Maher was sentenced to three months' of home confinement, whereas Salman was sent to prison for three years.

CONCLUSION

The judgment below should be reversed.

Respectfully submitted,

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STATUTORY APPENDIX

The Fifth Amendment to the United States Constitution provides in relevant part:

> No person shall...be deprived of life, liberty, or property, without due process of law....

U.S. CONST. amend. V

Section 10(b) of the Securities Exchange Act of 1934 provides:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange...
>
> (b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, or any securities-based swap agreement any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

15 U.S.C. §78j(b).

Securities and Exchange Commission Rule 10b–5 provides:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
>
> (a) To employ any device, scheme, or artifice to defraud,
>
> (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,
>
> in connection with the purchase or sale of any security

17 C.F.R. §240.10b–5.

Section 32(a) of the Securities Exchange Act of 1934 provides in relevant part:

> Any person who willfully violates any provision of this chapter...or any rule or regulation thereunder the violation of

> which is made unlawful or the observance of which is required under the terms of this chapter...shall upon conviction be fined not more than $5,000,000, or imprisoned not more than 20 years, or both, except that when such person is a person other than a natural person, a fine not exceeding $25,000,000 may be imposed; but no person shall be subject to imprisonment under this section for the violation of any rule or regulation if he proves that he had no knowledge of such rule or regulation.

15 U.S.C. §78ff(a).